



STOLL · KEENON · OGDEN
PLLC

300 WEST VINE STREET
SUITE 2100
LEXINGTON, KY 40507-1801
MAIN: (859) 231-3000
FAX: (859) 253-1093
www.skofirm.com

ROBERT M. WATT, III
DIRECT DIAL: (859) 231-3043
DIRECT FAX: (859) 246-3643
robert.watt@skofirm.com

June 7, 2011

HAND DELIVERED

Hon. Jeff Derouen
Executive Director
Public Service Commission
211 Sower Boulevard
P.O. Box 615
Frankfort, KY 40601

RECEIVED

JUN 07 2011

**PUBLIC SERVICE
COMMISSION**

Re: Delta Natural Gas Company, Inc.
Case No. 2011-00147

Dear Mr. Derouen:

Please find enclosed for filing an original and ten copies of the Application of Delta Natural Gas Company, Inc. for Approval of a Revised Gas Cost Recovery Tariff in the above-captioned case. Thanks in advance for your assistance.

Sincerely,

Robert M. Watt, III

rmw:

Enclosures

cc: Mr. John Brown (w/encl.)
Dennis Howard, II, Esq. (w/encl.)

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

RECEIVED

JUN 07 2011

PUBLIC SERVICE
COMMISSION

In the Matter of:

APPLICATION OF DELTA NATURAL)
GAS COMPANY, INC. FOR) CASE NO. 2011-00147
APPROVAL OF A REVISED GAS)
COST RECOVERY TARIFF)

* * * * *

APPLICATION

Pursuant to KRS Chapter 278 and the applicable sections of 807 KAR Chapter 5, Applicant, Delta Natural Gas Company, Inc. ("Delta"), respectfully states as follows:

1. The full name and mailing address of Delta are Delta Natural Gas Company, Inc., 3617 Lexington Road, Winchester, Kentucky 40391. Delta is a Kentucky corporation authorized to do business in the Commonwealth of Kentucky.

2. Delta is a utility engaged in the natural gas business. Delta purchases, sells, stores and transports natural gas in Bath, Estill, Montgomery, Menifee, Madison, Powell, Garrard, Jackson, Lee, Bourbon, Jessamine, Rowan, Bell, Knox, Whitley, Laurel, Clay, Leslie, Fayette, Fleming, Clark, Robertson and Mason Counties, Kentucky.

3. A Notice of Intent to file this Application was delivered to the Commission's Executive Director and to Kentucky's Attorney General on April 26, 2011. A copy of that Notice is attached hereto.

4. In the order dated October 21, 2010, in Case No. 2010-00116, *In the Matter of: Application of Delta Natural Gas Company, Inc. for an Adjustment of Rates*, the Commission

suggested that Delta look to its gas cost recovery mechanism to address its gas cost under-recoveries as opposed to its allowed return on equity.¹

5. Delta's proposed Gas Cost Recovery tariff, a copy of which is attached hereto, responds to the Commission's suggestion and is intended to prevent gas cost under-recoveries by the inclusion in the gas cost recovery rate of a GCR carrying cost, which compensates for the carrying cost associated with any under or over collections that have occurred as a result of prior adjustments.

6. Delta's application is supported by the testimonies of John B. Brown and Matthew D. Wesolosky, copies of which are attached hereto.

7. As required by KRS 278.030, the tariff proposed by Delta is fair, just and reasonable.

8. Delta proposes no effective date for the revised Gas Cost Recovery tariff, but requests that the Commission consider and act upon this Application in due course.

9. Delta further requests that the Commission continue in operation Delta's current Gas Cost Recovery tariff during the pendency of this case.

10. Notice to the public of the proposed tariff change has been given as prescribed in the Commission's regulation (807 KAR 5:011, Section 8), by including the notice in customer billings in accordance with the Commission's regulation (807 KAR 5:011, Section 8(2)(a)) and by exhibiting same for public inspection at the offices of Delta, 3617 Lexington Road, Winchester, Kentucky. A Certificate of Completed Notice will be filed with the Commission in the form recommended by Regulation, 807 KAR 5:011, Section 15(5).

¹ Order dated October 21, 2010, in Case No. 2010-00116, *In the Matter of: Application of Delta Natural Gas Company, Inc. for an Adjustment of Rates* at 21.

11. Delta also requests a deviation pursuant to 807 KAR 5:006(27) from any rule, regulation or other requirement that might otherwise delay or impede the review and approval of this Application.

12. Copies of all orders, pleadings and other communications related to this proceeding should be directed to:

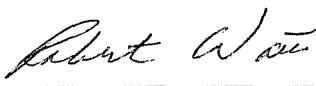
John B. Brown
Delta Natural Gas Company, Inc.
3617 Lexington Road
Winchester, KY 40391

Robert M. Watt, III
Stoll Keenon Ogden PLLC
300 West Vine Street, Suite 2100
Lexington, KY 40507

WHEREFORE, Delta Natural Gas Company, Inc. respectfully prays that its proposed Gas Cost Recovery tariff be approved as requested, that its current Gas Cost Recovery tariff continue in operation during the pendency of this case and for any and all other relief to which it may appear entitled.

Respectfully submitted,

Robert M. Watt, III
Stoll Keenon Ogden PLLC
300 West Vine Street, Suite 2100
Lexington, Kentucky 40507
(859) 231-3000
robert.watt@skofirm.com

By 
Counsel for Applicant

CERTIFICATE OF SERVICE

This is to certify that the foregoing pleading has been served by hand delivering a copy of same to the following person on this 7th day of June 2011:

Dennis Howard, II, Esq.
Lawrence W. Cook, Esq.
Assistant Attorneys General
Office of Rate Intervention
1024 Capital Center Drive
Frankfort, KY 40601



Counsel for Applicant



STOLL · KEENON · OGDEN
PLLC

300 WEST VINE STREET
SUITE 2100
LEXINGTON, KY 40507-1801
MAIN: (859) 231-3000
FAX: (859) 253-1093
www.skofirm.com

ROBERT M. WATT, III
DIRECT DIAL: (859) 231-3043
DIRECT FAX: (859) 246-3643
robert.watt@skofirm.com

April 26, 2011

HAND DELIVERED

RECEIVED

Hon. Jeff Derouen
Executive Director
Public Service Commission
211 Sower Boulevard
P.O. Box 615
Frankfort, KY 40601

APR 26 2011

**PUBLIC SERVICE
COMMISSION**

Re: Delta Natural Gas Company, Inc.

Dear Mr. Derouen:

We are counsel to Delta Natural Gas Company, Inc. ("Delta"). Please take notice that Delta intends to file on or after May 26, 2011, an application for approval of a change in its Gas Cost Recovery tariff.

Please assign this matter a case number and style and advise us of the same so that it can be incorporated into the application before it is filed with the Commission.

Should you have any questions, please contact me at your convenience.

Sincerely,

Robert M. Watt, III

rmw:

cc: Mr. John Brown

DETERMINATION OF GCR

The Company shall file a Quarterly Report with the Commission which shall contain an updated Gas Cost Recovery Rate (GCR) and shall be filed at least thirty (30) days prior to the beginning of each calendar quarter. The GCR shall become effective for billing with the final meter readings of the first billing cycle of each calendar quarter.

The gas cost recovery rates are comprised of:

- 1) The expected gas cost component (EGC), on a dollar per Ccf basis, which represents the average expected cost of gas supplies and may include fixed price, forward price and indexed price purchases. The purchases are less amounts injected into underground storage. The EGC includes withdrawals from underground storage at the average unit cost of working gas. The EGC includes the uncollectible gas costs portion of bad debt. In an effort to mitigate price volatility, the Company may contract with gas suppliers at fixed prices, at locked-in prices for gas to be delivered at future dates (forward price) and at index-based prices. These efforts can include the monthly or periodic layering of forward purchase volumes to help moderate the volatility of gas prices. The Company may consider published futures prices as well as price trends and price expectations at the time such decisions are made. Depending upon the circumstances, this volume can be up to the annual projected system requirements including storage needs.
- (2) The supplier refund adjustment (RA), on a dollar per Ccf basis, which reflects refunds received from suppliers during the reporting period, plus interest at the average 90 day commercial paper rate for the calendar quarter. In the event of any large or unusual refunds, the Company may apply to the Public Service Commission for the right to depart from the refund procedure herein set forth.
- (3) The actual adjustment (AA), on a dollar per Ccf basis, compensates for difference between the previous quarter's expected gas cost and the actual cost of gas during that quarter.
- (4) The balance adjustment (BA), on a dollar per Ccf basis, which compensates for any under or over collections which have occurred as a result of prior adjustments.
- (5) The GCR carrying cost (GCROC), on a dollar per Ccf basis, which compensates for the carrying cost associated with any under or over collections which have occurred as a result of prior adjustments.

BILLING

The gas cost recovery rate to be applied to bills of customers shall equal the sum of the following components:

$$\text{GCR} = \text{EGC} + \text{RA} + \text{AA} + \text{BA} + \text{GCRCC}$$

DEFINITIONS

For purposes of this tariff:

- (a) "Average Expected Cost" means the cost of gas supplies, adjusted for injections/withdrawals into storage and the uncollectible gas costs portion of bad debt. Cost of gas supplies include associated transportation and storage charges, and propane which results from the application of suppliers' rates currently in effect, or reasonably expected to be in effect during the calendar quarter, on purchased volumes during the twelve month period ending with the reporting period to which the GCR will apply, divided by the corresponding sales volume. Where the calculations require the use of volumes used during a given period, and those volumes did not exist for a particular source for the entire period, or the Company expects the volumes to change substantially, the Company may make appropriate adjustments in its calculations. Any adjustments of this type shall be described in the quarterly Gas Cost Recovery Report.
- (b) "GCR" means the quarterly updated gas cost recovery rate applicable to the monthly consumption of customers (sum of the expected gas cost component plus the supplier refund adjustment plus the actual adjustment plus the balancing adjustment plus the GCR carrying cost; i.e., $\text{GCR} = \text{EGC} + \text{RA} + \text{AA} + \text{BA} + \text{GCRCC}$).
- (c) "Calendar Quarters" means each of the four three-month periods of (1) August, September and October; (2) November, December and January; (3) February, March and April; and (4) May, June and July.
- (d) "Reporting Period" means the three (3) month accounting period that ended approximately sixty (60) days prior to the filing date of the updated gas recovery rates; i.e., the calendar quarter preceding that during which the most recent Quarterly Report was filed.

INTERIM GAS COST ADJUSTMENT FILINGS

The Company may make application for Interim Gas Cost Adjustments subject to the approval of the commission.

**COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION**

In the Matter of:

APPLICATION OF DELTA NATURAL)	
GAS COMPANY, INC. FOR APPROVAL)	CASE NO. 2011-00147
OF A REVISED GAS COST RECOVERY)	
TARIFF)	

DIRECT TESTIMONY OF

JOHN B. BROWN

AFFIDAVIT

The affiant, John B. Brown, being duly sworn, deposes and states that the prepared testimony attached hereto and made a part hereof, constitutes the prepared direct testimony of this affiant in Case No. 2011-00147, *In the Matter of: Application of Delta Natural Gas Company, Inc. for Approval of a Revised Gas Cost Recovery Tariff*, and that if asked the questions propounded therein, this affiant would make the answers set forth in the attached prepared direct testimony.

Affiant further states that he will be present and available for cross-examination and for such additional examination as may be appropriate at the hearing in Case No. 2011-00147 scheduled by the Commission, at which time affiant will further reaffirm the attached prepared testimony as his direct testimony in such case.

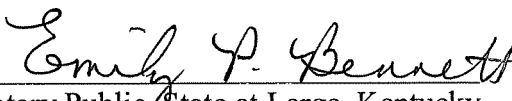


JOHN B. BROWN

STATE OF KENTUCKY)
)
COUNTY OF CLARK)

Subscribed and sworn to before me by John B. Brown, this the 6th day of June 2011.

My Commission Expires: 6/20/12



Notary Public, State at Large, Kentucky

1 **Q. Please state your name and business address.**

2 A. John B. Brown, Delta Natural Gas Company, Inc., 3617 Lexington Road, Winchester,
3 Kentucky40391.

4 **Q. What is your present employment?**

5 A. I am an accountant, presently employed by Delta as its Chief Financial Officer, Treasurer
6 and Secretary.

7 **Q. For what period of time have you been so employed?**

8 A. I was employed by Delta as Manager – Accounting & Finance in April of 1995. I was
9 appointed Controller in March of 1999 and promoted to Vice President – Controller and
10 Assistant Secretary in November, 2005. I was named Chief Financial Officer, Treasurer
11 and Secretary in May, 2007.

12 **Q. Would you briefly describe your education and professional experience?**

13 A. I attended Asbury College, Wilmore, Kentucky, from 1985 to 1989, receiving B.A.
14 degrees in accounting and business management with a minor in computer science. I
15 received an MBA degree from the University of Kentucky in 2000. I am a Certified
16 Public Accountant in the state of Kentucky. I was employed by the accounting firm of
17 Arthur Andersen LLP in its Louisville, Kentucky office from 1989 to 1995, specializing
18 in the utility area. Since April, 1995, I have been employed by Delta.

19 **Q. Generally what are your duties with Delta?**

20 A. As Chief Financial Officer, Treasurer and Secretary, I am responsible for finance,
21 treasury, budget, accounting, tax, internal audit, information technology, accounts
22 payable, human resources, rates, corporate governance and investor relations.

23 **Q. Are you generally familiar with the business affairs of Delta?**

1 A. Yes, I am.

2 **Q. Have you previously provided testimony to the Commission?**

3 A. Yes, I have been a witness on behalf of Delta in the following proceedings:

4 • Case No. 2010-00116, *Application of Delta Natural Gas Company, Inc. for an*
5 *Adjustment of Rates.*

6 • Case No. 2008-00062, *Application of Delta Natural Gas Company, Inc. for*
7 *Approval of a Customer Conservation/Efficiency Program and Demand Side*
8 *Management Cost Recovery Mechanism.*

9 • Case No. 2007-00089, *Application of Delta Natural Gas Company, Inc. for an*
10 *Adjustment of Rates.*

11 • Case No. 2004-00067, *Adjustment of the Rates of Delta Natural Gas Company, Inc.*

12 • Case No. 1999-176, *Adjustment of Rates of Delta Natural Gas Company, Inc.*

13 • Case No. 1997-066, *Adjustment of Rates of Delta Natural Gas Company, Inc.*

14 **Q. Please briefly summarize the scope of your testimony.**

15 A. My testimony relates to Delta's request to revise its GCR clause for allowed carrying
16 costs.

17 **Q. Why are you referencing Case No. 2010-00116 in this application?**

18 A. At page 21 of the Order dated October 21, 2010, in Case No. 2010-00116, Delta's last
19 general rate case, the Commission said, "Delta continues to ask for a higher return on
20 equity to address the problem of financing gas cost under-recoveries, but is unwilling to
21 take action to revise its GCR clause in ways that might substantially resolve this issue.
22 The Commission suggests once again that Delta look to its GCA mechanism as opposed

1 to its allowed ROE to address its gas cost under-recoveries.” This application is
2 responsive to the suggestions made in the Commission’s Order.

3 **Q. How has Delta developed its proposal?**

4 A. After receiving the Order, we designed a method for calculating the carrying costs
5 associated with unrecovered gas cost. We based the calculation on the method of
6 calculating carrying costs in Case No. 2010-00116 and prepared a revised Schedule I of
7 the Gas Cost Recovery calculation reflecting the addition of the GCR Carrying Cost
8 (GCRCC) component of rates. We requested an informal conference with the
9 Commission Staff to discuss our proposal. Several Delta and Staff representatives
10 participated in that conference held on February 24, 2011.

11 **Q. Please describe Exhibit 1.**

12 A. Exhibit 1 is a copy of Schedule I of the Gas Cost Recovery calculation, revised to include
13 a GCR Carrying Cost (GCRCC) component of rates. This schedule was provided and
14 discussed at the February 24, 2011, informal conference. The “GCR Carrying Cost
15 (GCRCC)” line was added in the “Particulars” section, and a “Carrying Cost of
16 Unrecovered Gas Cost” Section was added, which refers to Schedule VI, attached to my
17 testimony as Exhibit 2.

18 **Q. Please describe Exhibit 2.**

19 A. Exhibit 2 is a proposed Schedule VI to be added to the GCR filing, showing the
20 calculation of Carrying Cost of Unrecovered Gas Cost. This schedule was also provided
21 and discussed at the February 24, 2011 informal conference. In general, the balance of
22 Unrecovered Gas Cost is allocated based on capital structure. The amount allocated to
23 equity is multiplied by 10.4%, the same rate applied as the rate of return for common

1 equity at page 21 of the Order dated October 21, 2010, in Case No. 2010-00116, Delta's
2 last general rate case. The amount allocated to debt is multiplied by current debt rates.
3 After the tax gross up of equity component, an annual carrying cost is calculated. This
4 annual amount is converted to a quarterly amount by dividing by 4. The quarterly
5 amount is adjusted by the difference of actual carrying costs computed in the prior
6 quarter and the carrying cost billed through the GCRCC. Since the mechanism adjusts to
7 actuals on a quarterly basis, there are no additional balancing accounts required for the
8 GCRCC. The new GCRCC is set based on estimated sales for the quarter.

9 **Q Please describe Exhibits 3 and 4.**

10 A. Exhibits 3 and 4 are the same as Exhibits 1 and 2, except for the assumption that Delta
11 has over-recovered rather than being in an under-recovered position. These examples
12 show that the mechanism is symmetrical with respect to over- and under-recoveries.

13 **Q. What has Delta done as a result of the informal conference?**

14 A. The Staff members requested that they would like to consider a carrying cost recovery
15 mechanism like Delta proposed in conjunction with proposed modifications to the present
16 gas cost recovery calculation in hopes that over time, the Company would be better able
17 to more accurately estimate Unrecovered Gas Cost, thus minimizing the future impact of
18 the GCRCC. The Company committed to attempt to develop such proposed
19 modifications and has worked to refine the GCR calculations and assumptions in order to
20 do so.

21 **Q. Are you proposing additional changes as suggested by the Staff at the informal**
22 **conference?**

1 A. Yes. Delta has met internally several times since the informal conference, identifying
2 assumptions being used in the current GCR mechanism calculation which have tended
3 historically to cause the Company to under-estimate gas costs. See the testimony of
4 Matthew D. Wesolosky for a discussion of those suggested changes.

5 **Q. Do you believe that these suggested changes will completely solve the problem of**
6 **under-recovery?**

7 A. No. While modeling history shows that using the refined methodology significantly
8 improves the accuracy of the estimate of unrecovered gas cost, it is still an estimate that
9 could be materially inaccurate from one quarter to the next.

10 **Q. If you have identified refinements in the GCR mechanism that you believe will**
11 **result in lower unrecovered gas cost balances in the future, why does the Company**
12 **still need a GCRCC?**

13 A. As noted above, while we believe our refinements will improve our estimation results,
14 over- and under- recoveries will continue to exist, and carrying costs of those amounts
15 should be calculated on those amounts and collected from or remitted to the customers as
16 appropriate. Further, at March 31, 2011, the Actual Adjustment amount on the balance
17 sheet was \$3.4 million. Even if Delta is permitted to make the identified refinements in
18 the calculation, it will take several months for this balance to work down and the
19 Company should be allowed to recover carrying costs associated with that balance. In
20 addition, having the GCRCC in place protects the customer in the event any of the
21 changes to the mechanism result in an over-recovery position, the customers would have
22 their rates decreased by the carrying costs.

1 **Q. Are you proposing any other changes that would help prevent future under-**
2 **recoveries of this magnitude?**

3 A. Yes. Several times in the past, the Expected Gas Cost rate in the GCR filing has
4 decreased even when there has been a large under-recovered gas cost balance remaining.
5 From a common sense standpoint, even if future prices show declines, it does not make
6 sense to lower customer rates when a large under-recovered gas cost balance exists. Mr.
7 Wesolosky discusses in his testimony a control that simply requires that before an EGC
8 rate is decreased, the Company must be in an over-recovery position, and before an EGC
9 rate is increased, the Company must be in an under-recovery position. For instance, the
10 EGC rate effective July 26, 2010 was \$6.75. In successive quarters, the EGC was \$4.92,
11 \$5.15 and most recently, \$6.13. Had the proposed rate control been in effect, we would
12 have billed the EGC at \$6.75 through the winter and the unrecovered balance would
13 likely have been collected by now.

14 **Q. How do you suggest these proposals be implemented?**

15 A. For administrative ease, we request the Commission to order the Company to implement
16 the proposals for meter reads on and after a future GCR quarter beginning date. The
17 changes would then be reflected in the following normal GCR filing for the
18 Commission's review. The Company has not made and does not intend to make any of
19 the changes discussed in this proceeding to GCR filings until authorized by the
20 Commission.

21 **Q. Does this conclude your testimony at this time?**

22 A. Yes.

DELTA NATURAL GAS COMPANY, INC.

SCHEDULE I

GAS COST RECOVERY CALCULATION

COST RECOVERY RATE EFFECTIVE FEBRUARY __, 2010		
PARTICULARS	UNIT	AMOUNT
EXPECTED GAS COST (EGC)	\$/MCF	5.1463
SUPPLIER REFUND (RA)	\$/MCF	(0.0072)
ACTUAL ADJUSTMENT (AA)	\$/MCF	1.7354
BALANCE ADJUSTMENT (BA)	\$/MCF	(0.0225)
GCR CARRYING COST (GCRCC)	\$/MCF	0.0970
GAS COST RECOVERY RATE (GCR)	\$/MCF	6.9490

EXPECTED GAS COST SUMMARY CALCULATION

PARTICULARS	UNIT	AMOUNT
PRIMARY GAS SUPPLIERS (SCHEDULE II)	\$	6,986,450
UTILITY PRODUCTION	\$	-
INCLUDABLE PROPANE	\$	-
UNCOLLECTIBLE GAS COSTS	\$	118,264
	\$	7,104,714
TOTAL ESTIMATED SALES FOR QUARTER	MCF	1,380,537
EXPECTED GAS COST (EGC) RATE	\$/MCF	5.1463

SUPPLIER REFUND ADJUSTMENT SUMMARY CALCULATION

PARTICULARS	UNIT	AMOUNT
CURRENT QUARTER (SCHEDULE III)	\$/MCF	(0.0072)
PREVIOUS QUARTER	\$/MCF	-
SECOND PREVIOUS QUARTER	\$/MCF	-
THIRD PREVIOUS QUARTER	\$/MCF	-
SUPPLIER REFUND ADJUSTMENT (RA)	\$/MCF	(0.0072)

ACTUAL ADJUSTMENT SUMMARY CALCULATION

PARTICULARS	UNIT	AMOUNT
CURRENT QUARTER (SCHEDULE IV)	\$/MCF	0.5666
PREVIOUS QUARTER	\$/MCF	0.1852
SECOND PREVIOUS QUARTER	\$/MCF	(0.5276)
THIRD PREVIOUS QUARTER	\$/MCF	1.5112
ACTUAL ADJUSTMENT (AA)	\$/MCF	1.7354

CARRYING COST OF UNRECOVERED GAS COST

PARTICULARS	UNIT	AMOUNT
GCR CARRYING COST (GCRCC) (SCHEDULE VI)	\$/MCF	0.0970

BALANCE ADJUSTMENT SUMMARY CALCULATION

PARTICULARS	UNIT	AMOUNT
BALANCE ADJUSTMENT AMOUNT (SCHEDULE V)	\$	(31,007)
ESTIMATED SALES FOR QUARTER	MCF	1,380,537
BALANCE ADJUSTMENT (BA)	\$/MCF	(0.0225)

DELTA NATURAL GAS COMPANY, INC.

CARRYING COST OF UNRECOVERED GAS COST
AS OF OCTOBER 31, 2010

	Amounts	Ratios	Cost Rates	Weighted Cost of Capital	Allocated Unrecovered (Overrecovered) Gas Cost 10/31/10	Carrying Cost
Equity	59,907,869	48.59%	10.400%	5.054%	2,314,238	240,681
Long Term Debt	58,172,000	47.18%	6.833%	3.224%	2,247,182	153,558
Short Term Debt	<u>5,208,054</u>	4.22%	2.640%	<u>0.112%</u>	<u>201,187</u>	<u>5,311</u>
	<u>123,287,923</u>			<u>8.390%</u>	<u>4,762,607</u>	<u>399,550</u>
Equity portion of carrying cost				240,681		
Tax expansion factor, with PSC gross-up, per Case No. 2010-00116				<u>1.6065821</u>		
Equity portion of carrying cost, grossed up for income taxes				386,674		
Interest portion of carrying cost				<u>158,869</u>		
Annual carrying cost of unrecovered gas costs, grossed up for income taxes				545,543		
Quarterly carrying cost of unrecovered gas costs, grossed up for income taxes				136,386		
Prior quarter GCR carrying cost, grossed-up for income taxes				120,473		
Collections of prior quarter GCR carrying cost, grossed-up for income taxes				<u>(122,889)</u>		
Total				133,970		
Total estimated sales for the quarter (per Schedule II)			MCF	1,380,537		
GCR Carrying Cost Rate (GCRCC)			\$/MCF	<u>\$ 0.09704</u>		

Calculation of Cost Rates

Cost of Long Term Debt, October 31, 2010			
7.000%	Debentures	19,435,000	1,360,450
5.750%	Debentures	<u>38,737,000</u>	<u>2,227,378</u>
			3,587,828
	Debt Expense Amortization		<u>387,263</u>
	Annual Long Term Debt Expense		<u>3,975,091</u>
	Rate	<u>58,172,000</u>	<u>6.833%</u>
Cost of Short Term Debt, October 31, 2010 (rate as of 10/31/10)			
1.805%	Notes payable	5,208,054	94,005
0.125%	Unused line	34,791,946	<u>43,490</u>
	Annual Short Term Debt Expense		<u>137,495</u>
	Rate	5,208,054	<u>2.640%</u>

DELTA NATURAL GAS COMPANY, INC.

SCHEDULE I

GAS COST RECOVERY CALCULATION

COST RECOVERY RATE EFFECTIVE FEBRUARY __, 2010		
PARTICULARS	UNIT	AMOUNT
EXPECTED GAS COST (EGC)	\$/MCF	5.1463
SUPPLIER REFUND (RA)	\$/MCF	(0.0072)
ACTUAL ADJUSTMENT (AA)	\$/MCF	1.7354
BALANCE ADJUSTMENT (BA)	\$/MCF	(0.0225)
GCR CARRYING COST (GCRCC)	\$/MCF	(0.0970)
GAS COST RECOVERY RATE (GCR)	\$/MCF	6.7550

EXPECTED GAS COST SUMMARY CALCULATION

PARTICULARS	UNIT	AMOUNT
PRIMARY GAS SUPPLIERS (SCHEDULE II)	\$	6,986,450
UTILITY PRODUCTION	\$	-
INCLUDABLE PROPANE	\$	-
UNCOLLECTIBLE GAS COSTS	\$	118,264
	\$	7,104,714
TOTAL ESTIMATED SALES FOR QUARTER	MCF	1,380,537
EXPECTED GAS COST (EGC) RATE	\$/MCF	5.1463

SUPPLIER REFUND ADJUSTMENT SUMMARY CALCULATION

PARTICULARS	UNIT	AMOUNT
CURRENT QUARTER (SCHEDULE III)	\$/MCF	(0.0072)
PREVIOUS QUARTER	\$/MCF	-
SECOND PREVIOUS QUARTER	\$/MCF	-
THIRD PREVIOUS QUARTER	\$/MCF	-
SUPPLIER REFUND ADJUSTMENT (RA)	\$/MCF	(0.0072)

ACTUAL ADJUSTMENT SUMMARY CALCULATION

PARTICULARS	UNIT	AMOUNT
CURRENT QUARTER (SCHEDULE IV)	\$/MCF	0.5666
PREVIOUS QUARTER	\$/MCF	0.1852
SECOND PREVIOUS QUARTER	\$/MCF	(0.5276)
THIRD PREVIOUS QUARTER	\$/MCF	1.5112
ACTUAL ADJUSTMENT (AA)	\$/MCF	1.7354

CARRYING COST OF UNRECOVERED GAS COST

PARTICULARS	UNIT	AMOUNT
GCR CARRYING COST (GCRCC) (SCHEDULE VI)	\$/MCF	(0.0970)

BALANCE ADJUSTMENT SUMMARY CALCULATION

PARTICULARS	UNIT	AMOUNT
BALANCE ADJUSTMENT AMOUNT (SCHEDULE V)	\$	(31,007)
ESTIMATED SALES FOR QUARTER	MCF	1,380,537
BALANCE ADJUSTMENT (BA)	\$/MCF	(0.0225)

CARRYING COST OF UNRECOVERED GAS COST
AS OF OCTOBER 31, 2010

	Amounts	Ratios	Cost Rates	Weighted Cost of Capital	Allocated Unrecovered (Overrecovered) Gas Cost 10/31/10	Carrying Cost
Equity	59,907,869	48.59%	10.400%	5.054%	(2,314,238)	(240,681)
Long Term Debt	58,172,000	47.18%	6.833%	3.224%	(2,247,182)	(153,558)
Short Term Debt	<u>5,208,054</u>	4.22%	2.640%	<u>0.112%</u>	<u>(201,187)</u>	<u>(5,311)</u>
	<u>123,287,923</u>			<u>8.390%</u>	<u>(4,762,607)</u>	<u>(399,550)</u>
Equity portion of carrying cost				(240,681)		
Tax expansion factor, with PSC gross-up, per Case No. 2010-00116				<u>1.6065821</u>		
Equity portion of carrying cost, grossed up for income taxes				(386,674)		
Interest portion of carrying cost				<u>(158,869)</u>		
Annual carrying cost of unrecovered gas costs, grossed up for income taxes				(545,543)		
Quarterly carrying cost of unrecovered gas costs, grossed up for income taxes				(136,386)		
Prior quarter GCR carrying cost, grossed-up for income taxes				(120,473)		
Collections of prior quarter GCR carrying cost, grossed-up for income taxes				<u>122,889</u>		
Total				(133,970)		
Total estimated sales for the quarter (per Schedule II)			MCF	1,380,537		
GCR Carrying Cost Rate (GCRCC)			\$/MCF	<u>\$ (0.09704)</u>		

Calculation of Cost Rates

Cost of Long Term Debt, October 31, 2010			
7.000%	Debentures	19,435,000	1,360,450
5.750%	Debentures	<u>38,737,000</u>	<u>2,227,378</u>
			3,587,828
	Debt Expense Amortization		<u>387,263</u>
	Annual Long Term Debt Expense		<u>3,975,091</u>
	Rate	<u>58,172,000</u>	<u>6.833%</u>
Cost of Short Term Debt, October 31, 2010 (rate as of 10/31/10)			
1.805%	Notes payable	5,208,054	94,005
0.125%	Unused line	34,791,946	<u>43,490</u>
	Annual Short Term Debt Expense		<u>137,495</u>
	Rate	5,208,054	<u>2.640%</u>

**COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION**

In the Matter of:

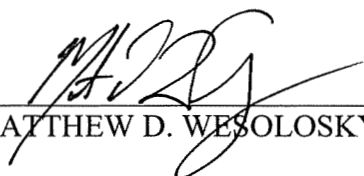
APPLICATION OF DELTA NATURAL)	
GAS COMPANY, INC. FOR APPROVAL)	CASE NO. 2011-00147
OF A REVISED GAS COST RECOVERY)	
TARIFF)	

**DIRECT TESTIMONY OF
MATTHEW D. WESOLOSKY**

AFFIDAVIT

The affiant, Matthew D. Wesolosky, being duly sworn, deposes and states that the prepared testimony attached hereto and made a part hereof, constitutes the prepared direct testimony of this affiant in Case No. 2011-00147, *In the Matter of: Application of Delta Natural Gas Company, Inc. for Approval of a Revised Gas Cost Recovery Tariff*, and that if asked the questions propounded therein, this affiant would make the answers set forth in the attached prepared direct testimony.

Affiant further states that he will be present and available for cross-examination and for such additional examination as may be appropriate at the hearing in Case No. 2011-00147 scheduled by the Commission, at which time affiant will further reaffirm the attached prepared testimony as his direct testimony in such case.

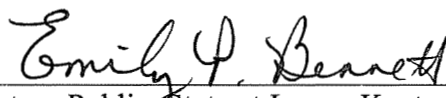


MATTHEW D. WESOLOSKY

STATE OF KENTUCKY)
)
COUNTY OF CLARK)

Subscribed and sworn to before me by Matthew D. Wesolosky, this the 15th day of June 2011.

My Commission Expires: 6/20/2012



Notary Public, State at Large, Kentucky

Q. Please state your name and business address.

A. My name is Matthew D. Wesolosky. My business address is 3617 Lexington Road, Winchester, Kentucky, 40391.

Q. By whom and in what capacity are you employed?

A. I am employed by Delta Natural Gas Company, Inc. as Vice President - Controller.

Q. Please describe your professional and educational background.

A. I received a Bachelor's of Science in Accounting from the University of Kentucky in 1999. I am a Certified Public Accountant in the State of Kentucky. From 1998 through 2001, I worked for at Delta. From 2001 through 2005 I worked in public accounting including two years at PricewaterhouseCoopers specializing in the utilities industry. I have worked at Delta since 2005.

Q. Generally, what are your duties with respect to Delta?

A. I manage the daily operations of the Accounting and Information Technology Departments.

Q. Have you testified previously before the Commission?

A. Yes, I have been a witness on behalf of Delta in the following proceedings:

Case No. 2010-00116, *Application of Delta Natural Gas Company, Inc. for an adjustment of rates,*

Case No. 2008-00062, *Application of Delta Natural Gas Company, Inc., for Approval of A Customer Conservation/Efficiency Program and Demand Side Management Cost Recovery Mechanism, and*

Case No. 2007-00089, *Application of Delta Natural Gas Company, Inc. For an Adjustment of Rates*

Q. What is the purpose of your testimony?

A. As noted in the testimony of John B. Brown, Delta requests recovery of the carrying costs associated with any over or under recovery of its gas cost. Delta has historically been in a significant under recovered position with respect to its gas costs. My testimony describes changes to the inputs and mechanics of the Gas Cost Recovery (“GCR”) mechanism Delta proposes to help reduce the amount of unrecovered gas cost and thus lower the carrying cost we seek to recover from our customers.

Q. What factors have given rise to Delta’s unrecovered gas cost?

A. The under-recovery of gas cost is due to shortfalls in our estimated gas cost (“EGC”) component of the GCR as compared to actual gas costs incurred. In reviewing historical GCR filings, Delta has noted that the estimated volumetric purchases by MCF, used as the denominator in calculating the EGC rate, is typically higher than actual sales by MCF. The estimated MCF purchases used in the EGC calculation has been calculated from operational data which is not necessarily comparable to sales data.

Q. What changes does Delta propose in its GCR mechanism to help reduce the under-recovery of gas costs?

A. Delta has evaluated its methodology for estimating MCF purchases used in the EGC calculation. Historically, operational data had been used to estimate the MCF purchases. Instead of using operational data, MCF purchases would be based on historical usage from our billing records, normalized for weather and adjusted from a billed month to a calendar month. Additionally, the conversion factor used to convert purchases from dekatherm (“DTH”) to MCF in the EGC calculation would be revised. Previously, this

conversion factor has been static, but going forward it would be updated on a quarterly basis to reflect the actual BTU content of Delta's system.

Q. How will these proposed changes help to reduce the under-recovery of gas costs?

A. Based on history, these changes will help to increase the denominator used in calculating the EGC rate to be more reflective of actual sales volumes which would help to reduce future Actual Adjustments.

Q. Does Delta propose any additional changes to the GCR mechanism to help reduce over or under recoveries?

A. Yes. Currently, each quarter Delta calculates a new EGC based on estimated purchases and volumes. Delta proposes adding a control to the mechanism where the effective EGC rate for a quarter would be the greater of the prior quarter's EGC or the current quarter's calculated EGC if Delta has a net under-recovery of its gas costs. Conversely, if Delta has a net over-recovery of its gas costs, the EGC would be the lesser of the calculated EGC or the subsequent quarter's EGC. The testimony of John B. Brown sets forth a practical example of how this control would function.

Q. Will these proposed changes to the GCR methodology ensure Delta has minimal over or under recoveries?

A. No, but it should reduce over- and under-recoveries. The EGC is truly an estimate. Factors which can impact how the EGC compares to actual gas costs include actual weather, which varies from normal, imbalances between Delta and its suppliers, as well as imbalances between Delta and its transportation customers.

Q. Will these proposed changes to the GCR enable Delta to collect through the GCR mechanism more than it pays for natural gas?

A. No. The GCR will still have the same balancing mechanisms which ensure that customers only pay for actual amount of gas purchased by Delta.

Q. Does this conclude your testimony at this time?

A. Yes.